



**State of Utah**  
GARY R. HERBERT  
*Governor*

SPENCER J. COX  
*Lieutenant Governor*

**Labor Commission**  
SHERRIE HAYASHI  
*Commissioner*

October 30, 2014

Governor Gary R. Herbert  
Senator Curtis S. Bramble  
Representative James A. Dunnigan

To Governor Herbert, Senator Bramble, Representative Dunnigan, and the members of the Business and Labor Interim Committee.

This is the fourth annual report from the Worker Classification Enforcement Council ("Council"), submitted pursuant to U.C.A. § 34-47-202. In the year since the Council's October 2013 report, the Council has continued to meet on a quarterly basis. Agenda and Minutes for all Council meetings are available on Utah's Public Notice Website.

Over the last year the Council has continued its efforts to increase communication and cooperation between Council member agencies. This has resulted in greater efficiency in investigating and addressing worker misclassification in Utah. Also, of note, the Labor Commission's misclassification hotline continues to produce referrals; the Department of Commerce has been involved in litigation relating to owner-worker model issues; the Department of Workforce Services has been recognized and awarded by the U.S. Department of Labor for superior performance in the area of worker misclassification detection and enforcement; and the Tax Commission's referrals have led to enforcement actions against those not complying with the law.

In the coming year the Council plans to expand its efforts to reach out to employers, human resources personnel, and accountants to help them understand misclassification issues and their obligations. The Council also plans to reach out to workers to help them understand their rights.

### **Regulatory and Law Enforcement Efforts, and the Status of Sharing Information by Member Agencies**

#### **The Labor Commission**

Since 2012 the Labor Commission has maintained a web page focused on worker misclassification issues in Utah. The web page defines employee misclassification, describes the negative impacts it can have across all facets of society, and educates the public on how to file a misclassification complaint with the Commission. The Commission also continues to monitor a misclassification hotline and has received a number of misclassification complaints through the hotline since its inception.

The Commission is charged with ensuring each employee in Utah is covered by workers' compensation insurance. The Commission's Industrial Accidents Division investigates each misclassification complaint to ensure the employer is providing workers' compensation coverage for its employees. The Division also investigates thousands of employers each year to ensure compliance with workers' compensation requirements, focusing on industries that tend to have higher rates of noncompliance, such as the construction industry, health services, and restaurant services. The Commission has assessed and collected a number of penalties against noncompliant employers based on misclassification complaints and referrals, as well as these internal investigations.

The Commission received 31 complaints of alleged misclassification through the hotline in the last year. After its investigation, the Industrial Accidents Division assessed penalties against 21 of these employers for failure to carry workers' compensation coverage. In the last year the Industrial Accidents Division also initiated investigations into a number of employers referred from the Department of Workforce Services and the Tax Commission, assessing penalties against 74 separate employers. The Commission also shares the misclassification complaints it receives, the results of subsequent investigations, and the results of its internal investigations with the members of the Council. This ability to share information between member agencies has been and continues to be critically important in addressing employee misclassification in Utah.

The Council has also explored ways to publicize the issue of misclassification and encourage misclassified workers to make complaints. In the coming months the Council will be reaching out to local media outlets, including Spanish-speaking outlets, to help workers understand their rights and employers understand their obligations. The Council will also explore partnerships with trade schools and technology colleges to help new graduates understand misclassification issues.

### **The Department of Commerce**

The Department of Commerce continues to focus its enforcement efforts on construction companies engaged in the owner-worker model and other methods of worker misclassification including: (1) contractors inappropriately paying workers as independent contractors rather than employees; and (2) contractors accepting cash payments to avoid payroll taxes and reporting to governmental agencies either as employees or independent contractors.

While the Department has reported investigative efforts involving companies using the owner-worker model, all but one known company have discontinued business or have relinquished their contractor licenses. The remaining company has multiple issues under evaluation in adjudicative proceedings including:

- (1) a substantial number of owner-workers who
  - (a) are not lawfully present,

- (b) have fraudulent social security cards,
  - (c) have a criminal history, or
  - (d) have judgments or tax liens filed against them;
- (2) unpaid fines against the company for OSHA safety violations;
- (3) unpaid fines against the predecessor companies for OSHA safety violations;
- (4) substantial discrepancies between the number of owner-workers the company reported on its reports filed with three different agencies,
- (5) substantial discrepancies in the reports of amounts paid to such owner-workers as reported on the company income tax returns as compared to report of earning for which unemployment insurance was paid for the owner-workers as reported to the Department of Workforce Services;
- (6) under-reporting of the number of owner-workers at the company;
- (7) underpayment of owner-worker reporting fees;
- (8) failure to comply with investigative subpoenas issued to owner-workers with questionable social security numbers; and
- (9) failure to comply with audit and reporting requirements.

The remaining company has filed five different lawsuits, attempting to challenge the investigations and agency actions taken against the company. These lawsuits address the following issues:

- (1) the constitutionality of requiring an owner-worker to be lawfully present in order to work in Utah;
- (2) citations issued to the company for having owner-workers who are not lawfully present and who provided fraudulent social security numbers;
- (3) the department's authority to issue investigative subpoenas requiring 153 owner-workers to produce original identity documents including social security cards, driver licenses, birth certificates, etc. These subpoenas were issued to owner-workers who have provided social security numbers that the Department has reason to believe may be false;
- (4) the constitutionality of Senate Bill 35 passed during the 2011 legislative session and Senate Bill 44 passed during the 2013 legislative session; and
- (5) a lawsuit which is an appeal of agency action taken against the company requiring the company to produce financial information of its owner-workers as required

by the Construction Trades Licensing Act or, alternatively, if the company does not comply with the audit and reporting requirement, revoking its contractor license.

The Attorney General's office is defending the Department of Commerce in each of these lawsuits.

The Department of Commerce continues to receive many referrals regarding contractors alleged to be hiring persons as independent contractors when the persons are acting as employees. The complainants allege that companies are paying persons in cash in order to avoid payroll tax obligations and reporting requirements, as well as to thwart the investigation and enforcement actions that may result.

The Department of Commerce continues to benefit from information exchanged through the Worker Classification Enforcement Council. This exchange of information with other agencies has assisted the Department of Commerce to take action against contractor licensees that are not complying with financial responsibility requirements. The Department of Commerce's actions against these contractors have assisted the Department of Workforce Services in its collection efforts for the Unemployment Insurance Fund.

### **The Department of Workforce Services**

The Department of Workforce Services Unemployment Insurance Division (DWS/UI) completes both "random" and "targeted" audits on Utah employers. In the last four and one-half year period, through June 30, 2014, DWS/UI completed 5,288 "random" audits, covering \$1.3 billion in total reported wages. The random audits identified approximately \$41 million in total unreported wages to 6,257 workers who were misclassified as "independent contractors," averaging \$7,753 in unreported earnings to 1.2 misclassified worker per random audit completed.

During the same period, DWS/UI completed 1,540 "targeted" audits of Utah employers, covering \$1.9 billion in total reported wages. These audits primarily use IRS Form 1099 information to identify potential unreported workers. The targeted audits identified over \$97 million in total unreported wages to 17,467 workers who were misclassified as independent contractors, averaging \$62,987 in unreported earnings to 11.3 misclassified workers per targeted audit completed.

The random and targeted audit results demonstrate that while the vast majority of registered Utah employers are reporting workers properly, a significant number of Utah employers are misclassifying their workers. In recent years, DWS/UI has focused more of its audit resources on targeted audits to increase employer compliance. The U.S. Department of Labor (DOL) provided guidance to all states' UI agencies in 2010 that worker misclassification detection and enforcement was a priority. States were advised that a new core performance outcome measure in the UI performance management system was created to help ensure states effectively used their audit resources to effectively detect employers that misclassify their employees. The new measure is

comprised of four factors: 1) Percent of Employers Audited Annually, 2) Percent of Total Wage Change From Audit, 3) Percent of Total Wages Audited, and 4) Average number of misclassifications Detected Per Audit. DWS's UI Division achieved a DOL determined effective audit score of 12.7 for the year ending December 31, 2013, surpassing the minimal acceptable score of 7.

Based on the effective audit measure score and other determining factors, Utah was recently awarded a \$327,974 "high performance bonus" grant by the U.S. Department of Labor. The bonus was provided for achieving superior performance in the area of worker misclassification detection and enforcement by the UI Contributions Field Audit team. Only four states qualified for this bonus; Utah achieved the second highest score nationally. This money will provide Utah with additional tools to increase its capabilities in collecting benefit overpayments and enhance our ability to audit large employers.

Over the last year, Department of Commerce and Labor Commission employees have worked with DWS/UI employees to expand access to the DWS/UI database. Now, Commerce employees can more effectively coordinate investigations when contractors are violating unemployment insurance laws. As a direct result of coordinated enforcement, DWS/UI collected \$811,513 in past-due contributions from 65 Utah employers in calendar year 2013. DWS/UI employees also referred dozens of unemployment insurance audits to Commerce, the Utah Tax Commission, and the IRS, identifying about 3,400 workers who were determined to be employees, not independent contractors. The Utah Tax Commission identified and referred numerous instances where employers issued Internal Revenue Service W-2 forms to employees that were not properly reported to DWS/UI.

The Council is placing an emphasis on community outreach in the coming months. DWS will coordinate participation in conferences to educate employers, accountants, and HR professionals on proper worker classification methods.

### **The Tax Commission**

The Tax Commission benefits from the Worker's Classification Enforcement Council due to the many referrals it receives from the Council member agencies. The Commission has a very successful exchange of information with the Department of Workforce Services. DWS sends the Commission referrals on employers that they have registered or for which they have reclassified their workers and the Tax Commission sends DWS referrals on employers not registered with DWS. The Tax Commission is limited on the information it can share with the Council. Nevertheless, the Commission does benefit from the information that is shared from the Council.

### **Recommended Legislative Changes**

The Council appreciates the attention the Legislature has given to worker classification issues. The Council has no specific recommendations for the 2015 legislative session.

We look forward to continuing to report annual progress, and are glad to provide any other requested information or answer any questions.

Sincerely,



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cc: Senator Karen Mayne